Report

of the

Examination of

Old Republic Mercantile Insurance Company

Brookfield, Wisconsin

As of December 31, 2002

TABLE OF CONTENTS

State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

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Jorge Gomez, *Commissioner*

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October 30, 2003

Honorable Jorge Gomez
Commissioner of Insurance
State of Wisconsin
125 South Webster Street
Madison, Wisconsin 53702

Commissioner:

In accordance with your instructions, a compliance examination has been made of the affairs and financial condition of:

OLD REPUBLIC MERCANTILE INSURANCE COMPANY
BROOKFIELD, WISCONSIN

and this report is respectfully submitted.

I. INTRODUCTION

The previous examination of Old Republic Mercantile Insurance Company (hereinafter, also “ORMIC” or “the company”) was conducted in 1998 as of December 31, 1997. The current examination covered the intervening period ending December 31, 2002, and included a review of such 2003 transactions as deemed necessary to complete the examination.

The examination consisted of a review of all major phases of the company's operations, and included the following areas:

History
Management and Control
Corporate Records
Conflict of Interest
Fidelity Bonds and Other Insurance
Employees' Welfare and Pension Plans
Territory and Plan of Operations
Affiliated Companies
Growth of Company
Reinsurance
Financial Statements
Accounts and Records
Data Processing

Emphasis was placed on the audit of those areas of the company's operations accorded a high priority by the examiner-in-charge when planning the examination. Special attention was given to the action taken by the company to satisfy the recommendations and comments made in the previous examination report.

The section of this report titled "Summary of Examination Results" contains comments and elaboration on those areas where adverse findings were noted or where unusual situations existed. Comments on the remaining areas of the company's operations are contained in the examination work papers.

The company is annually audited by an independent public accounting firm as prescribed by s. Ins 50.05, Wis. Adm. Code. An integral part of this compliance examination was the review of the independent accountant's work papers. Based on the results of the review of these work papers, alternative or additional examination steps deemed necessary for the completion of this examination were performed. The examination work papers contain documentation with respect to the alternative or additional examination steps performed during the course of the examination.

Independent Actuary's Review

Independent actuaries were engaged under a contract with the Office of the Commissioner of Insurance (OCI). They reviewed the adequacy of the company's loss reserves and loss adjustment expense reserves. The results of their work were reported to the examiner-in-charge. As deemed appropriate, reference is made in this report to the actuaries' conclusion.

II. HISTORY AND PLAN OF OPERATION

Old Republic Mercantile Insurance Company was incorporated under the laws of the state of Mississippi on November 11, 1985, and commenced business on the same date. The company redomiciled to Arizona on November 29, 1988, and from Arizona to Wisconsin on December 7, 1995.

The company has its origins in NN Risk Management, Inc., an underwriting management company that placed specialty commercial risks with its affiliate, Northwestern National Insurance Company. Old Republic International Corporation (hereinafter also "ORI") acquired NN Risk Management, Inc., in 1985. After acquisition, NN Risk Management, Inc., was dissolved. The role of NN Risk Management, Inc., was then assumed by Old Republic Risk Management, Inc. (hereinafter also "ORRM").

ORRM designs risk management programs to assist major U.S. and Canadian industrial corporations, service organizations, and governmental entities in meeting their commercial insurance needs. These programs include the use of captive insurers, large deductibles, retrospective rating, and other alternative market approaches to risk management. The programs must make provision for accounting, claims, inspection, and other services, the combination of which depends on the specific risk management strategy selected. Each program is customized to fit the specific needs of each client. Historically, ORRM has given particular emphasis to industrial and manufacturing firms having a net worth of at least $100,000,000.00.

Because ORRM or its affiliates provide services critical to the success of the client's risk management program, clients often wish to assure incentive for good performance by having an affiliated insurer take some portion of the risk. ORMIC was originally organized to function as a profit center for ORI to track the results of the specialty risk management programs designed by ORRM.

Old Republic Mercantile Insurance Company was capitalized by an intermediate downstream holding company of ORI, known as Old Republic Northern Holdings, Inc. (hereinafter also, "ORNHI"). ORNHI was established as a means to reward executives responsible for the financial results of Old Republic Risk Management, Inc., and Old Republic

Mercantile Insurance Company should their guidance in the initial years of these two companies profit ORI. ORMIC was a wholly owned subsidiary of ORNHI. Interest in the common shares of ORNHI was apportioned 80% to Old Republic General Insurance Group, Inc., and 20% to the selected key executives. Pursuant to a stock subscription and purchase agreement, participating executives may exchange their common shares for cash or common shares of ORI. On July 1, 1996, all the executives exchanged their common shares resulting in ORI owning 100% of ORNHI.

Effective February 27, 1998, ORRM became the surviving entity in a merger with Old Republic Northern Holdings, Inc., while assuming the name of its former parent. With the merger, Old Republic General Services, Inc., held all of the issued and outstanding shares of ORRM, and the subsidiaries of ORNHI became the subsidiaries of ORRM including ORMIC. This merger and the expanded responsibilities of ORRM management have raised the corporation's financial and operational profile. Additional information concerning the holding company system is contained in the section of this report captioned, "Affiliated Companies".

The company acts exclusively as a reinsurer. Since its inception, the company has had one reinsurance contract which was been amended three times. The original reinsurance treaty (including the first amendment) with Old Republic Insurance Company (hereinafter also "ORIC") dealt with all insurance policies written in conjunction with the programs designed by ORRM, which were written by ORIC, and to a lesser extent, International Business and Mercantile Reassurance Company (hereinafter also, "IB&M Re"). ORIC and IB&M Re ceded some or all of the risks so acquired to some combination of captive reinsurers or nonaffiliated reinsurers. Until January 1, 1997, any portion of the risk not ceded to either captive reinsurers or nonaffiliated reinsurers was ceded to ORMIC. An amendment to its reinsurance contract effective January 1, 1997 (second amendment), ORMIC's role was narrowed in scope. ORMIC accepted a portion of the excess layer on many ORRM programs (of upper reinsurance layers or shared layers on a semiautomatic facultative basis). While ORMIC's participation percentage on the excess layers varied from policy to policy, its risk on any one policy generally did not exceed $200,000 per policy year. ORMIC no longer participated on the "first dollar" portion of newly written risks due to that amendment. (Prior to this change, the company assumed commercial risks and related assigned risk participations which ORIC did not place with other nonaffiliated reinsurers.) The treaty was further amended effective May 28, 1999, to eliminate the acceptance of any net retained liability from ORIC for policies that were effective prior to January 1, 1997, as well as to eliminate IB&M Re as one of the ceding companies.

While the methodologies vary, alternative risk mechanisms entail self-insurance of most, or all, of the risk so placed. The role of ORIC as the fronting insurance underwriter may be viewed as analogous to that of a surety, ultimately insuring the performance of obligations existing between the corporate policyholder and third parties. Accordingly, ORIC's underwriters, acting through ORRM, monitor each insured's financial profile and seek to maintain security or other form of collateral protection equal to the actuarially determined reserves for losses, loss adjustment expenses, and unearned premium. Currently, one of ORI's goals is to keep ORMIC's licenses active, which they achieve by ceding business to it. To satisfy the needs of customers and/or reinsurers, the ORI Group's retention of business could occur within ORIC, therefore ORMIC's existence is not essential to ORRM's business activity.

The company has no office properties, direct lease obligations, or employees of its own. The company's home office is the Milwaukee branch office of the ORIC, and ORIC's Milwaukee staff perform most day-to-day operations in accordance with ORIC's business practices and internal controls. ORIC personnel located in Chicago, Illinois, Saddle Brook, New Jersey, and Greensburg, Pennsylvania supplement the marketing activities of the Milwaukee branch.

Most of the underlying new business reinsured, in part, by ORMIC is acquired through brokers hired by potential clients. Compensation for such brokers is negotiated between broker and client, and is paid by the client, not by ORRM or ORMIC. In-house marketing personnel at ORIC also gain clients through direct contacts with the risk managers of large organizations. The complexity inherent in this business and the competitive struggle for such large accounts is such that only a handful of new clients are gained each year. Retention of existing clients is particularly important for growth over time.

ORIC and ORMIC do not directly handle claims on behalf of alternative risk management programs. Instead, claims are administered by some 79 third-party administrators, which work for ORIC under written claims services agreements. Contracts with third-party administrators are established and renewed on a policy-by-policy basis. Generally, the insured selects its own claims administrator(s) from ORRM's list of approved contractors. In some instances, insureds administer their own claims through their own technically qualified claim departments.

ORIC selectively performs audits throughout each year of third-party administrators from its approved list. These audits emphasize the credibility of claim file information, the sufficiency of case reserves, and the accuracy with which information is transmitted to ORIC. ORRM tracks the losses incurred in each accident year on a year-to-date and inception-to-date basis, by client and by claim administrator.

The company gets involved in claims only when a loss approaches the excess layer it reinsures. The claims department of the ORIC's Milwaukee branch track case files on the company's behalf. Claim files consist of copies of third-party administrator claim files for large loss cases. Such claims almost always involve severe worker's compensation claims involving a chemical or industrial accident.

Except for licensing and other regulatory fees, nearly all expenses are initially paid on the company's behalf by an affiliate, Old Republic General Services, Inc. Expenses other than taxes are then allocated on the basis of specific identification or time estimates in accordance with a written service agreement. Tax allocations are established in accordance with a federal income tax-sharing agreement by and between ORI and the insurers of its General Insurance Group. intercompany balances with affiliates are created in the ordinary course of business, with settlements generally made on a monthly or quarterly basis, depending on the type of transaction. Written agreements with affiliates are further described in the section of this report titled "Affiliated Companies".

As of the examination date, the company was licensed in Arizona, Oregon, Pennsylvania, and Wisconsin.

In the state of Wisconsin, the company is licensed to transact the following lines of business as defined by s. Ins 6.75 (2), Wis. Adm. Code:

(a) Fire, Inland Marine, and Other Property
(b) Ocean Marine
(c) Disability
(d) Liability and Incidental Medical Expense
(e) Automobile and Aircraft
(k) Worker's Compensation
(n) Miscellaneous

The following table is a summary of the net insurance premiums written by the company in 2002. The growth of the company is discussed in the Financial Data section of this report.

Line of Business	Direct Premium	Reinsurance Assumed	Reinsurance Ceded	Net Premium
Reinsurance - non-proportional assumed liability	$0	$1,651,502	$0	$1,651,502

The following table is a comparative summary of gross premiums written in 1997 and 2002. The growth of the company is discussed in the Financial Data section of this report.

Product Line	1997 Premium	2002 Premium	% Change in Premium
Nonproportional reinsurance	$9,267,013	$1,651,502	(82.0)%

The reason for the significant decline in premium volume since the prior examination is explained in Section VI of this report under the caption, "Growth of Old Republic Mercantile Insurance Company."

III. MANAGEMENT AND CONTROL

Control by Succession of Parent Corporations

Old Republic International Corporation holds ultimate control of the company's board and of its executive direction. As more thoroughly described both previously and in Section IV, "Affiliated Companies," of this report, ORI indirectly, but wholly, owns all issued and outstanding common shares of the company. Accordingly, ORI effectively controls the nomination and election of the board of directors.

Board of Directors

The board of directors consists of five members. All directors are elected annually to serve a one-year term. Officers are elected at the board's annual meeting. Most of the directors, as executive employees of the holding company system, receive no compensation specific to their service on the board. Members of the company's board of directors are typically members of other boards of directors in the holding company system. Officers are elected at the board's annual organizational meeting, and as positions are created or fall vacant.

Currently, the board of directors consists of the following persons:

Name and Residence	Principal Occupation	Term Expires
John S. Adams Wilmette, Illinois	Senior Vice-President and Chief Executive Officer Old Republic International Corporation	2002
Lawrence J. Francione Brookfield, Wisconsin	Vice-President and Chief Financial Officer Old Republic Risk Management, Inc.	2002
James A. Kellogg Brookfield, Wisconsin	President Old Republic General Insurance Group of Old Republic International Corporation	2002
Spencer A. LeRoy, III La Grange, Illinois	Senior Vice-President, Secretary and General Counsel Old Republic International Corporation	2002
Aldo C. Zucaro Barrington, Illinois	Chairman of the Board, President and Chief Executive Officer Old Republic International	2002

Officers of the Company

The officers serving at the time of this examination are as follows:

Name	Office	2002 Compensation
Aldo C. Zucaro	Chairman of the Board	
James A. Kellogg	President	
Spencer A. LeRoy, III	Vice President, Secretary and General Counsel	
Charles S. Boone	Senior Vice President and Treasurer	
John S. Adams	Senior Vice President and Chief Financial Officer	
Lawrence J. Francione	Vice President, Assistant Secretary and Assistant Treasurer	
Barry T. Marin	Vice President	
Fred M. Savaglio	Vice President and Assistant Treasurer	
Michael R. Weber	Executive Vice President	

The company did not provide this office with its executives' compensation for 2002. Comments are made in the "Report of Executive Compensation" section of this report.

Committees of the Board

The company's bylaws allow for the formation of certain committees by the board of directors. There are currently no board committees, however, there was an executive committee appointed in 1998 for a one year term. This will be discussed further in the "Summary of Examination Results" section of this report.

IV. AFFILIATED COMPANIES

Old Republic Mercantile Insurance Company is a member of a holding company system led by Old Republic International Corporation (hereinafter also, “Old Republic holding company system”). The organizational chart below depicts the relationships among the affiliates in the group. The organizational chart follows a brief description of the holding company structure and significant affiliates.

Old Republic International Corporation is one of the 50 largest publicly held insurance organizations in the United States, with a substantial interest in a diversified range of insurance and reinsurance services. ORI holds direct or indirect ownership or majority control over 94 corporations, excluding inactive or otherwise financially insignificant entities. The holding company system does not conduct significant operations outside of the United States and Canada. While various offshore entities belong to the Old Republic holding company system, such corporations exist to facilitate the management of U.S. and Canadian based risks. The entire emphasis of the Old Republic holding company system is on insurance and activities incidental to or in support of the distribution of insurance.

The Old Republic holding company system conducts its operations through four operational groups, consisting of the General Insurance Group, the Mortgage Insurance Group, the Title Insurance Group, and the Life Insurance Group. The General Insurance Group provides commercial lines of property and liability insurance and reinsurance, predominantly to industrial, mining, transportation, and financial services companies, as well as actuarial consulting, tax planning, claims control, and management of captive or retrospectively rated insurance programs. The Mortgage Insurance Group provides residential mortgage guaranty insurance for first mortgage loans to mortgage bankers, commercial banks, thrifts, credit unions, and other financial institutions. The Title Insurance Group provides title insurance and related real estate transfer services for individuals, businesses, and government entities. The primary emphases of the Life Insurance Group are on marketing credit life and disability insurance products through automobile dealers, and providing large-face-amount term life insurance products through a network of independent life brokerage general agencies. They also sell specialty life and health products through lenders, travel agents, and educational institutions.

Within these four broad segments, ORI and its subsidiaries have sought to act as a niche player specializing in a relatively limited number of industries or lines of insurance. Growth has been sought through methodical progress within the specific industries and product niches to which the Old Republic holding company system has committed itself.

ORMIC may be regarded as a member of a distinct holding company subsystem within the General Insurance Group, consisting of Old Republic Insurance Company, Old Republic Risk Management, Inc., ORMIC, and Remington General Assurance Ltd. These entities assist major U.S. and Canadian industrial, service, and governmental entities in meeting their basic commercial insurance needs through the use of captive insurers, large deductible programs, retrospective rating, and other alternative market approaches to risk management. Marketing is principally through independent brokers, and, to a lesser extent, in-house sales staff.

Present Succession of Control

Old Republic International Corporation

Old Republic International Corporation is a Chicago-based multiple lines insurance holding company incorporated under the laws of Delaware on March 10, 1969. ORI's common shares are publicly traded on the New York Stock Exchange. One outstanding class of preferred stock, the Series G Convertible Preferred, exists to support the corporation's employee stock option plan and does not trade, though it is convertible into common shares under certain restrictive terms and conditions. On a consolidated basis for the fiscal year ending December 31, 2002, ORI reported assets of $8,715,400,000, liabilities and preferred stock of $5,559,500,000, total common shareholders' equity of $3,155,800,000, total revenues of $2,756,400,000, and a net income of $392,900,000.00.

Old Republic General Insurance Group, Inc.

Old Republic General Insurance Group, Inc. (hereinafter also "ORGIG"), was incorporated in Delaware on December 3, 1979. This wholly owned subsidiary of ORI is the leading holding company of ORI's General Insurance Group, exercising direct or indirect ownership or effective control over 35 corporations, excluding inactive or otherwise financially insignificant entities. The General Insurance Group is the most significant operating division within the Old Republic holding company system and contains the greatest diversity in terms of the lines of business written and scope of ancillary insurance activities. ORGIG's consolidated statutory financial statement as of December 31, 2002, reported assets of $4,021,564,588, liabilities of $2,743,505,059, common shareholder's equity of $1,278,059,528, and net income of $112,295,283.00.

Old Republic Risk Management, Inc.

Old Republic Risk Management, Inc., was incorporated under the laws of the state of Delaware on July 2, 1985. ORRM, based in Brookfield, Wisconsin, specializes in the design and supervision of alternative market risk management programs for large industrial, service, and government entities in the United States and Canada. The four most common approaches to client needs include use of captive insurers, large deductible programs, retrospective rating, and self-insurance combined with an excess of loss reinsurance plan. All business ORMIC assumes from ORIC originates from alternative market programs designed and underwritten by ORRM. As of December 31, 2002, the corporation reported assets of $16,326,965, liabilities of $10,427,346, and common shareholder's equity of $5,899,619.00. The corporation reported net revenues of $2,377,911 and a net loss of ($87,770) for 2002.

ORRM has no employees of its own. All personnel necessary to conduct the day-to-day activities of ORRM are employees of ORIC. ORRM functions as ORIC's Milwaukee branch. In 1997, the responsibilities of ORRM management were expanded to include supervision of alternative risk management activities conducted from ORIC branches in Chicago, Illinois, and Greensburg, Pennsylvania. Premium derived from programs produced by ORRM approximate 36% of ORIC's overall business.

Significant Affiliates

This section addresses affiliated companies that are not in the "succession of control" section above, but with which the company has some business relationship.

Old Republic Asset Management Corporation

Old Republic Asset Management Corporation (hereinafter also "ORAM"), organized as an Illinois corporation on January 28, 1966, provides investment management services to the members of the Old Republic holding company system, including ORMIC, pursuant to written agreements. The corporation was initially known as Trinity Insurance Agency, Inc. In March 1980, the corporate title was changed to that presently used in reflection of the change in its purpose and scope of activities. The corporation has no employees of its own rather it utilizes those of ORIC. Functionally, it serves as a cost allocation center for accounting control purposes. ORAM is a wholly owned second-tier subsidiary of ORI. As of December 31, 2002, the corporation reported assets of $363,924, liabilities of $78,687, common shareholder's equity of $363,924 total revenues of $1,667,704, and net income of $236,363.00.

Old Republic General Services, Inc.

Old Republic General Services, Inc. (hereinafter also "ORGS"), organized as an Illinois corporation on July 20, 1960, provides various general and administrative services for members of the Old Republic holding company system, including ORMIC. Services include, but are not limited to, accounting, records management, tax preparation, legal activity, and data processing. Services of this type are provided pursuant to written service agreements. The corporation has no employees of its own rather it utilizes those of ORIC. Functionally, it serves the same purpose as ORAM, except for different categories of expense. The corporation was formerly known as R. E. Flannery & Associates, Inc. In 1978, the corporate title was changed to that presently used in reflection of the change in its purpose and scope of activities. ORGS is a wholly owned second-tier subsidiary of ORI. As of December 31, 2002, the corporation reported assets of $4,200,950, liabilities of $4,219,815, common shareholder's equity of ($18,865) total revenues of $9,815,854, and net income of $92,918.00.

Old Republic Insurance Company

Old Republic Insurance Company was incorporated under the laws of the Commonwealth of Pennsylvania on April 11, 1935, and commenced business on April 21, 1935. Interests identified with various coal companies and allied industrial concerns organized the corporation under the title, “Coal Operators Casualty Company”. On April 18, 1955, the Old Republic holding company system acquired control of the corporation from its original sponsors, and on June 7 of the same year, changed the name to that presently used.

ORIC is the lead carrier and primary employer in ORI’s General Insurance Group. ORIC’s marketing efforts are concentrated on large commercial accounts with specialized insurance requirements. It is licensed in all 50 U.S. states, the District of Columbia, Guam, Puerto Rico, and the U.S. Virgin Islands. On its 2002 statutory annual statement, ORIC reported net admitted assets of $1,589,636,000, liabilities of $1,053,198,000, policyholders’ surplus of $536,439,000, and net income of $44,402,000.00.

Remington General Assurance Ltd.

Remington General Assurance Ltd. is a Bermuda-domiciled captive insurer incorporated on April 28, 1982. It is marketed as a means for clients of ORRM to gain the advantages of the off-shore captive structure without the commitment of capital and administrative expense required to establish their own captive. Through reinsurance, funds held by the captive on behalf of multiple clients are segregated by client and any underwriting profit or investment income ultimately accrues back to the client. ORRM, with staff provided by ORIC, provides underwriting, claims management, and loss control services. As of December 31, 2002, the corporation reported assets of $2,524,938, liabilities of $775,169, and common shareholder’s equity of $1,749,769. In 2002, the corporation reported revenues of $111,852 and a net loss of ($99,127.00).

Subsequent to the date of this report, Remington General Assurance Ltd., was transferred from ORRM to ORGIG on February 20, 2003. As part of this transfer, Remington General Assurance Ltd’s name changed to Old Republic Reassurance Ltd., effective April 1, 2003.

Organizational Chart
As of December 31, 2002

Old Republic International Corporation (DE)	"ORI"
Old Republic General Insurance Group, Inc. (DE)	"ORGIG"
Old Republic Insurance Company (PA)	"ORIC"
Old Republic Risk Management, Inc. (DE)	"ORRM"
Old Republic Mercantile Insurance Company (WI)	"ORMIC"
Remington General Assurance, Ltd. (Bermuda)	
Old Republic Asset Management Corporation (IL)	"ORAM"
Old Republic Marketing, Inc. (IL)	
Old Republic General Services, Inc. (IL)	"ORGS"

Note that the above organizational chart is a modification of the original due to the complexity of the group's structure. The examiner included only affiliates that directly effect the operations of Old Republic Mercantile Insurance Company. The acronym used in this report is also shown.

Agreements with Affiliates

As previously noted, the company has no employees of its own. All day-to-day operations are conducted with staff provided by ORIC in accordance with the business practices and internal controls it maintains with respect to its employees. In addition to common staffing and management control by ORIC, ORMIC's relationship to its affiliates is affected by four written agreements. Reinsurance agreements are described in the reinsurance section of this report. A brief summary of the other three agreements follows, with the arrangement in chronological order.

Tax-Sharing Agreement

ORMIC became party to a federal income tax-sharing agreement by and between ORI and its ORGIG subsidiaries through an addendum to this agreement dated March 14, 1986. This agreement neutralizes any advantage or disadvantage as a result of the consolidation of federal income taxes. If any party's federal income tax liability, as computed on a separate return basis without regard to consolidation, is less than its allocated share under consolidation, ORI is to reimburse that party for the deficiency. If any party's federal income tax liability, as computed on a separate return basis without regard to consolidation, is greater than its allocated share under consolidation that party is to reimburse ORI in an amount equal to the gain. ORI is obligated to render statements for settlement under this agreement within 30 days after the applicable federal income tax filing. Unless the subsidiary objects, settlement is to occur within 15 days of receipt of the statement. This agreement may be cancelled at the end of any taxable year with 30 days' advance written notice.

Service Agreement

Effective January 1, 1988, the company entered into a service agreement with ORGS. Under this agreement, ORGS agrees to perform the following services in compliance with all applicable laws and regulations:

A. Prepare all books and records including financial records, reports, and correspondence with regulatory authorities;

B. Maintain and store all records and supplies of ORMIC;

C. Prepare the annual statement, quarterly statements, and income tax returns of ORMIC;

D. Make payments of accounts payable and other obligations, and receipt for and deposit funds payable, and account for such transactions in ORMIC's books and records;

E. Prepare insurance and reinsurance statements and reinsurance contracts;

F. Provide computer services and computer time as necessary to perform functions contracted in this agreement;

G. Perform other duties as agreed upon from time-to-time by the parties.

ORMIC is to compensate ORGS at its regular billing rate for hours worked plus expenses incurred. This contract may be cancelled at any time by mutual agreement, or unilaterally by either party with 180 days' advance written notice to the other.

Investment Counsel Agreement

Effective October 1, 1995, the company entered into an investment counsel agreement with Old Republic Asset Management Corporation. Under this agreement, ORAM is to act as investment counsel, advising the company on investment policy, executing purchases and sales of investments as instructed by company, monitor the value of its invested assets, and preparing investment statements for insurance regulatory purposes on a quarterly basis. This agreement may be terminated by either party at the end of any quarterly investment period upon

30 days' advance notice. The fee for services provided by ORAM is a sliding scale percentage that declines as assets under management increase. ORMIC is to pay ORAM the following quarterly fee based on assets under management at the date the fee is assessed. It should be noted that this agreement was amended, effective April 1, 2002, to adjust the fee to what is now being currently charged ORMIC.

Net Portfolio Assets	**Quarterly Fee**	**Annualized Quarterly Fee**
Minimum Fee	$500	$2,000
First $100,000,000	1.75 basis points	7 basis points
Next $150,000,000	1.25 basis points	5 basis points
Over $250,000,000	0.75 basis points	3 basis points

In 2002, ORMIC incurred $7,419 in fees for investment counsel and services rendered by ORAM.

V. REINSURANCE

The company has had only one reinsurance contract since its inception, which has been amended three times. This affiliated assuming contract includes proper insolvency provisions, and is summarized below.

Affiliated Assuming Contracts

1.	Type:	Facultative Excess of Loss Reinsurance Treaty
	Reinsured:	Old Republic Insurance Company
	Scope:	Reinsured may cede the upper or shared layers of property and casualty excess of loss risks on a semiautomatic facultative basis.
	Retention:	The retention may vary on a risk-by-risk basis.
	Coverage:	The reinsurer's participation on the upper layer excess of loss risks assumed varies on a risk-by-risk basis.
	Premium:	Reinsurance premiums are determined on a risk-by-risk basis, but are proportional to other participants in the same excess of loss layer.
	Commissions:	Ceding commissions are calculated by adding the following items: a) Compensation paid to ORRM by the reinsured for all costs incurred by ORRM; b) Premium taxes, fees and assessments payable to states, boards, bureaus, associations and guarantee funds caused by the reinsured's writing of the insurance ceded hereunder; c) 0.5% of the insurance premium ceded hereunder; d) The reinsurance premium net of ceding commission paid or due on all other reinsurance ceded hereunder which inures to the benefit of the reinsurer by reducing the risk ceded hereunder.
	Effective date:	July 1, 1985, as amended effective October 1, 1992, January 1, 1997, and April 1, 1999.
	Termination:	Any party to this treaty may terminate their participation at the end of any calendar month with 180 days' written notice.

VI. FINANCIAL DATA

The following financial statements reflect the financial condition of the company as reported to the Commissioner of Insurance in the December 31, 2002, annual statement. Also included in this section are schedules that reflect the growth of the company, NAIC Insurance Regulatory Information System (IRIS) ratio results for the period under examination, and the compulsory and security surplus calculation. Adjustments made as a result of the examination are noted at the end of this section in the area captioned "Reconciliation of Surplus per Examination."

Old Republic Mercantile Insurance Company
Assets
As of December 31, 2002

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$ 9,717,225	$0	$ 9,717,225
Cash	4,293		4,293
Short-term investments	363,938		363,938
Federal and foreign income tax recoverable and interest thereon	438,966		438,966
Interest, dividends, and real estate income due and accrued	154,784		154,784
Receivable from parent, subsidiaries, and affiliates	133,710		133,710
Total Assets	$10,812,916	$0	$10,812,916

Old Republic Mercantile Insurance Company
Liabilities, Surplus, and Other Funds
As of December 31, 2002

Losses		$ 7,369,536
Loss adjustment expenses		202,951
Other expenses (excluding taxes, licenses, and fees)		30,700
Total Liabilities		7,603,187
Common capital stock	2,000,000	
Gross paid in and contributed surplus	1,000,000	
Unassigned funds (surplus)	209,729	
Surplus as Regards Policyholders		3,209,729
Total Liabilities and Surplus		$10,812,916

Old Republic Mercantile Insurance Company
Summary of Operations
For the Year 2002

Underwriting Income		
Premiums earned		$1,651,502
Deductions:		
Losses incurred	$2,023,085	
Loss expenses incurred	43,085	
Other underwriting expenses incurred	204,858	
Total underwriting deductions		2,271,028
Net underwriting gain or (loss)		(619,526)
Investment Income		
Net investment income earned	612,796	
Net realized capital gains or (losses)	2	
Net investment gain or (loss)		612,798
Net income (loss) before federal and foreign income taxes		(6,728)
Federal and foreign income taxes incurred		206,123
Net Loss		$ (212,851)

Old Republic Mercantile Insurance Company
Cash Flow
For the Year 2002

Premiums collected net of reinsurance			$1,651,502
Deduct:			
Loss and loss adjustment expenses paid (net of salvage or subrogation)			273,512
Underwriting expenses paid			199,526
Other underwriting (income) expenses			66,410
Cash from underwriting			1,112,054
Net investment income			605,728
Deduct:			
Federal income taxes paid (recovered)			366,763
Net cash from operations			1,351,019
Proceeds from investments sold, matured, or repaid:			
Bonds	$ 858,000		
Total investment proceeds		858,000	
Cost of investments acquired (long-term only):			
Bonds	1,796,885		
Total investments acquired		1,796,885	
Net cash from investments			(938,885)
Cash applied for financing and miscellaneous uses:			
Dividends to stockholders paid	300,000		
Total		300,000	
Net cash from financing and miscellaneous sources			(300,000)
Reconciliation			
Net change in cash and short-term investments			112,134
Cash and short-term investments, December 31, 2001			256,097
Cash and short-term investments, December 31, 2002			$ 368,231

Old Republic Mercantile Insurance Company
Compulsory and Security Surplus Calculation
December 31, 2002

Assets		$10,812,916
Less liabilities		7,603,187
Adjusted surplus		3,209,729
Annual premium:		
Lines other than accident and health	$1,651,502	
Factor	100%	
Compulsory surplus (subject to a minimum of $2 million)		2,000,000
Compulsory surplus excess (or deficit)		$ 1,209,729
Adjusted surplus (from above)		$ 3,209,729
Security surplus: (140% of compulsory surplus, factor reduced 1% for each $33 million in premium written in excess of $10 million, with a minimum factor of 110%)		2,800,000
Security surplus excess (or deficit)		$ 409,729

Old Republic Mercantile Insurance Company
Reconciliation and Analysis of Surplus
For the Five -Year Period Ending December 31, 2002

The following schedule is a reconciliation of total surplus during the period under examination as reported by the company in its filed annual statements:

	2002	2001	2000	1999	1998
Surplus, beginning of year	$3,788,104	$3,579,578	$13,059,543	$33,154,241	$44,339,256
Net income	(212,851)	338,871	519,799	7,913,280	8,814,985
Net unrealized capital gains or (losses)	(32,027)	(76,941)	236	(7,978)	
Change in net deferred income tax	(33,497)	172,447			
Cumulative effect of changes in accounting principles		74,149			
Capital changes:					
Paid in			(1,000,000)		
Surplus adjustments:					
Paid in			(1,000,000)		
Dividends to stockholders	(300,000)	(300,000)	(8,000,000)	(28,000,000)	(20,000,000)
Surplus, end of year	$3,209,729	$3,788,104	$3,579,578	$13,059,543	$33,154,241

Old Republic Mercantile Insurance Company
Insurance Regulatory Information System
For the Five-Year Period Ending December 31, 2002

The company's NAIC Insurance Regulatory Information System (IRIS) results for the period under examination are summarized below. Unusual IRIS results are denoted with asterisks and discussed below the table.

	Ratio	2002	2001	2000	1999	1998
#1	Gross Premium to Surplus	51.0%	19.0%	20.0%	8.0%	0.0%
#2	Net Premium to Surplus	51.0	19.0	20.0	8.0	0.0
#3	Change in Net Writings	127.0*	0.0	(27.0)	999.0*	(99.0)*
#4	Surplus Aid to Surplus	0.0	0.0	0.0	0.0	0.0
#5	Two-Year Overall Operating Ratio	75.0	0.0	0.0	0.0	0.0
#6	Investment Yield	6.5	6.7	6.6	4.2*	6.6
#7	Change in Surplus	(15.0)*	6.0	(73.0)*	(61.0)*	(25.0)*
#8	Liabilities to Liquid Assets	74.0	63.0	64.0	34.0	75.0
#9	Agents' Balances to Surplus	0.0	0.0	0.0	0.0	0.0
#10	One-Year Reserve Devel. to Surplus	7.0	0.0	0.0	(2.0)	(11.0)
#11	Two-Year Reserve Devel. to Surplus	(3.0)	(1.0)	(2.0)	(13.0)	7.0
#12	Estimated Current Reserve Def. To Surplus	(174.0)*	(18.0)	(31.0)	0.0	(99.0)

Ratio #3 measures the change in the company's net writings from the previous years. In 1997 and 1998, net premiums written decreased by 69% and 139%, respectively. In 1997, the company's business operations changed so that it assumes only excess of loss business from affiliates. Prior to 1997, in addition to excess losses, the company assumed quota share commercial risk business and the related assigned risk participation. The exceptional result in 1998 was due to an even more reduced participation in assigned risk pools, and a decrease in premiums from retrospectively adjustable policies for large commercial risk business assumed. April 1, 1999, the company entered into a termination, retrocession, and commutation agreement, which coincided with a facultative reinsurance agreement with ORIC, that was previously mentioned, where the company assumes the upper reinsurance layers or shared layers on a semiautomatic facultative basis from ORIC, which it in turn entirely retained. The reduced business in 1997 and 1998, which resulted in negative net premiums written in 1998, combined with the increase in ceded business from ORIC, due to the revised reinsurance agreement previously mentioned, caused this ratio to be exceptional in 1999. The exceptional result in 2002 directly relates to the increased amount of business that was ceded to the company from ORMIC, which can be attributed in part to general market increases in direct premium rates and in the cost of reinsurance in 2002.

Ratio #6 measures the amount of the company's net investment income as a percentage of the average amount of cash and invested assets it had during the year. The exceptional result in 1999 was primarily due to a reduction in its invested assets resulting from the transfer of cash and securities in settlement of the commutation mentioned in the previous section. Special cash dividends of $20 million and $28 million for 1998 and 1999 respectively were given to ORIC as part of the commutation previously mentioned. The reductions of the company's invested asset base combined with the market conditions in 1999 reduced its earning power.

Ratio #7 measures the change in the company's policyholders' surplus from the previous year. The exceptional results in 1998, 1999, and 2000 were due to the changes in assumed reinsurance to only upper reinsurance layers or shared layers on a semiautomatic facultative basis, and paying extraordinary dividends, filed with and approved by this office. The exceptional result in 2002 was due to the reduction of surplus caused by the company's largest underwriting loss since inception.

Ratio #12 compares the company's loss reserves and loss ratios for the past two years. This is performed by taking the company's loss reserves and dividing them by the earned premium for the last two-years resulting in a ratio of 790% (including development), which is the main contributing factor in the calculation that is causing this IRIS ratio to be exceptional. The reason for the significant loss ratios for the past two years was caused by significant adverse development of prior years' reserves. However, as discussed later in this report, the office's consulting actuary found that the company's current reserves appear to be adequately stated.

Growth of Old Republic Mercantile Insurance Company

Year	Admitted Assets	Liabilities	Surplus As Regards Policyholders	Net Income
2002	$10,812,916	$7,603,187	$3,209,729	($212,851)
2001	9,593,301	5,805,197	3,788,104	338,871
2000	9,899,944	6,320,366	3,579,578	519,799
1999	19,642,607	6,583,064	13,059,543	7,913,280
1998	131,766,941	98,612,701	33,154,240	8,814,985
1997	156,101,029	111,761,776	44,339,253	7,620,471

Year	Gross Premium Written	Net Premium Written	Premium Earned	Loss And LAE Ratio	Expense Ratio	Combined Ratio
2002	$1,651,502	$1,651,502	$1,651,502	125.1%	12.4%	137.5%
2001	728,438	728,438	728,438	90.3	15.9	106.2
2000	725,838	725,838	725,838	90.0	14.9	104.9
1999	997,254	997,254	997,254	6.5	21.4	27.9
1998	(3,627,893)	(3,627,893)	(3,445,577)	105.6	27.3	132.7
1997	9,267,013	9,267,013	10,976,053	100.3	6.2	106.5

The company's gross and net premiums written were identical throughout the period under examination because the company does not reinsure any portion of the risks it assumes from its affiliates. As noted in a previous section of the report, the dramatic decline in premiums in 1998 was the result of a significant change in its reinsurance agreement effective in 1998.

The 1998 changes to ORMIC's business plan have had a clear impact on the company's written premiums, loss and loss adjustment expense ratio, expense ratio, and net income. The company's written premiums over the last three years reflect increases in excess loss business on large commercial risks assumed from ORIC. The loss ratio increased as losses on run-off were spread over a smaller premium base. The expense ratio and net income declined as a result of the reduced level of business activity.

Reconciliation of Surplus per Examination

No adjustments were made to reported surplus as a result of the examination.

Examination Reclassifications

	Debit	Credit
Receivable from parent, subsidiaries and affiliates		$133,710
Premiums and agents' balances in course of collection	$456,431	
Reinsurance payable on paid loss and LAE		282,829
Commissions payable, contingent commissions and other similar charges		39,892
Total reclassifications	$456,431	$456,431

VII. SUMMARY OF EXAMINATION RESULTS

Compliance with Prior Examination Report Recommendations

There were 15 specific comments and recommendations in the previous examination report. Comments and recommendations contained in the last examination report and actions taken by the company are as follows:

1. Plan of Operation—It is recommended that the company maintain an up-to-date business plan with Wisconsin's Office of the Commissioner of Insurance (OCI) until December 31, 2000, pursuant to s. 611.28, Wis. Stat.

   Action—Compliance

2. Corporate Records—It is recommended that the company amend its articles of incorporation and bylaws as necessary to reflect practices of corporate governance accurately and to remain in accord with statutory requirements.

   Action—Noncompliance, see comments in the summary of current examination results.

3. Reinsurance Treaty Trust Account Agreement—It is recommended that the company amend the Reinsurance Treaty Trust Account Agreement to require Old Republic Insurance Company to provide at least 30 days notice prior to any material withdrawal from the trust. It is further recommended that the company provide at least 30 days notice to the Commissioner prior to any such withdrawal of assets from the trust.

   Action—Compliance

4. Reinsurance Treaty Trust Account Agreement—It is recommended that the company notify OCI at least 30 days prior to writing direct business or entering into any new reinsurance treaty, pursuant to s. 601.42, Wis. Stat. This recommendation is to apply only until such time as the Reinsurance Treaty Trust Account Agreement in terminated.

   Action—Compliance

5. Reinsurance Treaty Trust Account Agreement—It is recommended that the company consider termination of the Reinsurance Treaty Trust Account Agreement on the basis that the original purpose or which it was established is no longer applicable.

   Action—Compliance

6. Collateral Security—It is recommended that the company file a list of security by account and a status report of security relative to security required for reinsured risks as supplements to future statutory financial statements. Each such report made pursuant to this recommendation is required under s. 601.42, Wis. Stat., and each such report is privileged under s. 601.465, Wis. Stat.

   Action—Compliance

7. Collateral Security—The company is advised that the Commissioner may make adjustments to compulsory and security surplus requirements to reflect the specific circumstances of individual insurers pursuant to s. 623.11, Wis. Stat., and s. 623.12, Wis. Stat.

   Action—Compliance

8. Collateral Security—It is recommended that the company amend its reinsurance contract with ORIC and IB&M Re to state that the company cannot indemnify for losses occasioned by the failure or insufficiency of any letter of credit that does not extend to successors of the beneficiary by operation of law.

   Action—Compliance

9. Losses and Loss Adjustment Expenses—It is recommended that the company direct its appointed actuary to expand the breadth of the actuarial analysis undertaken in support of statutorily required statements of actuarial opinion to include studies of captive business, even if such studies are subject to extensive qualification.

   Action—Compliance

10. Losses and Loss Adjustment Expenses—It is recommended that future actuarial opinions or supporting work papers include comment on the materiality of the nonreviewed exposures or otherwise explain the rationale for declining to review selected lines of business.

    Action—Compliance

11. Losses and Loss Adjustment Expenses—It is recommended that future actuarial reports include written documentation of the calculations used to arrive at the selected ULAE reserve.

    Action—Compliance

12. Losses and Loss Adjustment Expenses—It is recommended that future actuarial reports include a comparison of reserves indicated by actuarial analysis and those carried by the company.

    Action—Compliance

13. Other Expenses—It is recommended that the company cease to pay expenses on behalf of its parent and affiliates absent written agreements providing for full and timely reimbursement, pursuant to s. 611.61 (1) (b), Wis. Stat.

    Action—Compliance

14. Assumed Reinsurance Balances Payable—It is recommended that the company maintain a system of recordkeeping that does not leave it vulnerable to the sudden departure of key personnel.

    Action—Compliance

Summary of Current Examination Results

Report of Executive Compensation

Each Wisconsin domiciled insurer is required to file a supplemental schedule to its annual filed financial statement entitled, “Report of Executive Compensation”, pursuant to s. 601.42, Wis. Stat., and s. 611.63 (4), Wis. Stat. This report requires insurers to report the direct or allocated total annual compensation paid to each director, the chief executive officer, and the four most highly compensated officers or employees other than the chief executive officer. In addition, the report requires disclosure of the compensation of all officers and employees whose compensation exceeds specified amounts. For an insurer of ORMIC’s size, the compensation of each officer or employee whose annual compensation exceeds $80,000 is to be reported.

As mentioned in Section III of this report (Management and Control), management of the company is performed by officers of other companies in the Old Republic Group. Due to the reduced business operations of ORMIC only a small portion of the directors’ and executive officers’ compensation is allocated to the company. The company therefore believes that providing this information is not relevant. The company therefore did not provide this information as part of its 2002 Annual Statement filing. It is recommended that the company properly complete the “Report of Executive Compensation”, as required by s. 601.42, Wis. Stat., and s. 611.63 (4), Wis. Stat.

Corporate Records

According to Article III, Section 10 of the company’s bylaws, the board of directors is required to designate an executive committee consisting of one or more directors. Review of the company's board minutes disclosed that the board of directors never appointed an executive committee as required by its bylaws. This was a finding and recommendation in the prior examination of the company. It is therefore again recommended that the company amend its articles of incorporation and bylaws as necessary to reflect practices of corporate governance accurately and to remain in accord with statutory requirements.

The examiners reviewed all biographical data for the company's officers and directors filed with this office. It was noted that four out of the six officers' and directors' biographical data had not been filed. This information was requested during examination fieldwork and the company could not provide proof that the biographical data was filed with this office. It is recommended that the company comply with s. Ins 6.52, Wis. Adm. Code, concerning the filing of biographical data of its officers and directors with the Office of the Commissioner of Insurance OCI).

Invested Assets

Section 610.23, Wis. Stat., requires insurers to hold all investments and deposits of its funds in its own name except that:

> (1) Securities kept under a custodial agreement or trust arrangement with a bank or banking and trust company may be issued in the name of a nominee of the bank or banking and trust company; and
>
> (2) Any insurer may acquire and hold securities in bearer form.

The company is in compliance with these requirements. However, the company's safekeeping agreement with its custodian does not contain the proper indemnification language prescribed in the NAIC's Financial Condition Examiners Handbook. The provisions prescribed by the handbook are as follows:

a) That the bank or trust company as custodian is obligated to indemnify the insurance company for any loss of securities of the insurance co. in the bank or trust company's custody occasioned by the negligence or dishonesty of the bank or trust company's officers or employees, or burglary, robbery, holdup, theft, or mysterious disappearance, including loss by damage or destruction;

b) That in the event that there is a loss of the securities for which the bank or trust company is obligated to indemnify the insurance company, the securities shall be promptly replace or the value of the securities and the value of any of rights or privileges resulting from said loss of securities shall be promptly replaced;

It is recommended that the company amend its custodial agreement to include proper indemnification language prescribed in the NAIC's Financial Condition Examiners handbook.

Federal and Foreign Income Tax Recoverable **$438,966**

This asset represents the balance refundable at year-end for federal income taxes. This balance was calculated by netting the company's deferred tax assets, deferred tax liabilities, and current income tax liability. Review of the company's deferred tax asset calculation found that the non-admitted portion of the deferred tax asset was not included in the filed annual statement in column 1 of the assets page, and was not reported as non-admitted in column 2 of that page, and the non-admitted portion was not disclosed in the gains and losses in surplus schedule on page 4. The net admitted portion of the asset is not affected by this non-disclosure so an adjustment to surplus was not necessary. However, it is recommended that the company disclose the non-admitted portion of the deferred tax asset calculation in future annual statement filings in accordance with the NAIC Annual Statement Instructions – Property & Casualty and SSAP #10 in the NAIC Accounting Practices and Procedures Manual.

Receivable from Parent, Subsidiary and Affiliates **$0**

The original liability of $133,710 represents the net amount due to the company from its affiliates at December 31, 2002. Review of this balance revealed that this asset consisted of a net affiliated reinsurance settlement balance, which was inappropriately reported in this account. The net affiliated reinsurance settlement balance included a reinsurance premiums receivable balance of $456,431, a reinsurance payable on paid losses and LAE balance of $282,829, and a commissions payable balance of $39,892, all of which should have been included as separate line items on the balance sheet in accordance with NAIC Annual Statement Instructions – Property & Casualty. It is recommended that the company properly report affiliated reinsurance balances in future annual statement filings in accordance with the NAIC Annual Statement Instructions – Property & Casualty as follows:

- Reinsurance premium receivable balance is to be reported on the premiums and agents' balances in course of collection line;
- Reinsurance payable on paid losses & LAE balance is to be reported on the reinsurance payable on paid losses and LAE line;
- Reinsurance commissions payable balance is to be reported on commissions payable, contingent commissions and other similar charges line.

Reclassifications have been made in the “Reconciliation of Surplus per Examination” section of this report to reflect the above finding.

Unpaid Losses and Unpaid Loss Adjustment Expenses $7,369,536 and $202,951

These liabilities represent the company’s estimate of amounts payable on losses incurred and loss adjustment expenses incurred on or prior to December 31, 2002, and remaining unpaid as of that date. As noted earlier, independent actuaries engaged by the Office of the Commissioner of Insurance (OCI) reviewed the adequacy of the company’s loss reserves and loss adjustment expense reserves. The independent actuaries determined that the company’s current reserves were adequately stated.

VIII. CONCLUSION

Policyholders' surplus has decreased significantly during the period under review from $44,339,253 as of year-end 1997, to $3,209,729 as of year-end 2002. This represents a decrease of 92.8% during the period under examination, and is largely due to a major change in the company's business plans that resulted in dividend payments to its parent totaling over $58 million during this period. The examination found that the company, despite the large decrease in surplus meets its financial requirements under s. 623.11, Wis. Stat., and s. 623.12, Wis. Stat.

The examination of Old Republic Mercantile Insurance Company resulted in five recommendations, one repeated from the prior examination and one reclassification. The reclassification and its corresponding recommendation was due to the company improperly reporting affiliated reinsurance balances as a net amount on the receivable from parent, subsidiary and affiliates line on its filed balance sheet. The other recommendations pertain to statutory reporting requirements, proper annual statement filing requirements and compliance with technical aspects of corporate governance.

There was a significant change in the company's reinsurance program during the examination period. Effective April 1, 1999, the company entered into a termination, retrocession and commutation agreement with Old Republic Insurance Company. The implementation of this agreement resulted in the reduction of premium and liability ceded to ORMIC. ORIC in return received assets and liabilities of approximately $91 million as a result of the retrocession and commutation. Currently, the company's business is limited to a facultative reinsurance agreement with ORIC where it assumes a portion of the upper reinsurance layers or shared layers on a semiautomatic facultative basis. The company retains the entire amount of risk it assumes from ORIC.

The company's original business purpose as the profit center for tracking the results of specialty risk management programs is no longer applicable. Currently, the company's operational plan is to maintain the licenses it currently has by assuming business from ORIC. The company does not have any current plans to write direct business.

IX. SUMMARY OF COMMENTS AND RECOMMENDATIONS

1. Page 32 - Report of Executive Compensation—It is recommended that the company properly complete the "Report of Executive Compensation", as required by s. 601.42, Wis. Stat., and s. 611.63 (4), Wis. Stat.

2. Page 32 Corporate Records—It is therefore again recommended that the company amend its articles of incorporation and bylaws as necessary to reflect practices of corporate governance accurately and to remain in accord with statutory requirements.

3. Page 33 - Corporate Records—It is recommended that the company comply with s. Ins 6.52, Wis. Adm. Code, concerning the filing of biographical data of its officers and directors with the Office of the Commissioner of Insurance OCI).

4. Page 33 - Invested Assets—It is recommended that the company amend its custodial agreement to include proper indemnification language prescribed in the NAIC's Financial Condition Examiners handbook.

5. Page 34 - Federal and Foreign Income Tax Recoverable—It is recommended that the company disclose the non-admitted portion of the deferred tax asset calculation in future annual statement filings in accordance with the NAIC Annual Statement Instructions – Property & Casualty and SSAP #10 in the NAIC Accounting Practices and Procedures Manual.

6. Page 34 - Receivable from Parent, Subsidiary and Affiliates—It is recommended that the company properly report affiliated reinsurance balances in future annual statement filings in accordance with the NAIC Annual Statement Instructions – Property & Casualty as follows:

    - Reinsurance premium receivable balance is to be reported on the premiums and agents' balances in course of collection line;

    - Reinsurance payable on paid losses & LAE balance is to be reported on the reinsurance payable on paid losses and LAE line;

    - Reinsurance commissions payable balance is to be reported on commissions payable, contingent commissions and other similar charges line.

X. ACKNOWLEDGMENT

The courtesy and cooperation extended during the course of the examination by the officers and employees of the company are acknowledged.

In addition to the undersigned, the following representatives of the Office of the Commissioner of Insurance (OCI), State of Wisconsin, participated in the examination:

Name	Title
Jerry C. DeArmond	Insurance Financial Examiner Advanced Loss Reserve Specialist
Cruz J. Flores	Insurance Financial Examiner Advanced Data Processing Audit Specialist
Tom M. Janke	Insurance Financial Examiner
Russel L. Lamb	Insurance Financial Examiner
Frederick H. Thornton	Insurance Financial Examiner Advanced Exam Planning & Quality Control Specialist
Sheur Yang	Insurance Financial Examiner

Respectfully submitted,

John E. Litweiler
Examiner-in-Charge

XI. SUBSEQUENT EVENTS

On March 1, 2004, this office received the company's December 31, 2003, Annual Statement filing. The company's RBC ratio of 176% fell below the company action level of 200%. The company will file an RBC action plan by April 15, 2004. The company is considering commuting all contracts with its affiliates and dissolving by year-end 2004.